UNITED STATES BANKRUPTCY COURT

CENTRAL DISTRICT OF ILLINOIS

In Re	)	
	)	In Bankruptcy
THOMAS L. FOLDER,	)	
	)	Case No. 99-70292
Debtor.	)	
_____	)	
	)	
LAWRENCE SEMENZA and NANCY SEMENZA,	)	
	)	
Plaintiffs,	)	
	)	
v.	)	Adversary No. 99-7035
	)	
THOMAS L. FOLDER,	)	
	)	
Defendant.	)	

O P I N I O N

The issue before the Court is whether a Consent Order of Prohibition executed by the Defendant in a Secretary of State administrative proceeding collaterally estops the Defendant from re-litigating the issues which were resolved by the Consent Order of Prohibition.

The material facts are not in dispute. Cen-Com Internet of Illinois was an Illinois Business Corporation offering internet access to subscribers. The Defendant, Thomas Folder, was the President, Chief Executive Officer, and majority shareholder of Cen-Com.

In 1996, a number of lawsuits were filed against the Defendant and Cen-Com. In addition, on June 27, 1996, the Illinois

Department of Revenue served a Notice of Levy on Cen-Com's depository bank.

In January, 1996, the Plaintiff, Dr. Lawrence Semenza, telephoned the Defendant and arranged a tour of the Cen-Com facilities. Upon arriving at the Cen-Com business office, the Plaintiffs were furnished with a copy of the Cen-Com Internet Business Plan. The Business Plan projected net earnings for the 1996 fiscal year in excess of $8 million. In addition, the Defendant advised the Plaintiffs that Cen-Com was a fast-growing company with "hubs" in most major cities in the United States.

On July 3, 1996, and July 30, 1996, the Defendant offered and sold two promissory notes in the total amount of $40,000 to the Plaintiffs. The notes were secured by the Defendant's Cen-Com stock.

Three days after execution of the July 30 note, Cen-Com filed a petition pursuant to Chapter 11 of the Bankruptcy Code.

On December 10, 1996, the Illinois Secretary of State, Securities Division, filed a three-count complaint against the Defendant individually and Cen-Com pursuant to Section 11.F of the Illinois Securities Law of 1933 (815 ILCS 5/1, *et seq.*) and 14 Ill. Adm. Code 130, Subpart K. Count I of the complaint alleged omission of a material fact, Count II alleged misrepresentation of a material fact, and Count III alleged fraud or deceit.

On February 14, 1997, the Defendant and the Illinois Secretary of State executed a Stipulation to Enter Consent Order of Prohibition wherein the Defendant stipulated to the following

facts:

f. That Cen-Com and Folder failed to disclose to the Semenza's (sic) that it had lost a significant amount of customer accounts in June 1996;

g. That Cen-Com and Folder failed to disclose to the Semenza's (sic) that they had several lawsuits pending against them at the time the promissory notes were offered and sold to the Semenza's (sic);

h. That Cen-Com and Folder failed to disclose to the Semenza's (sic) that Cen-Com, or its corporate predecessor, had received notices of tax liens from the Illinois Department of Revenue and the Internal Revenue Service and a Notice of Determination and Demand for Payment from the Illinois Department of Employment Services;

i. That Cen-Com and Folder failed to disclose to the Semenza's (sic) that Cen-Com was preparing to file a Bankruptcy petition at the time it sold the July 30, 1996 promissory note to the Semenza's (sic)(.)

A Consent Order of Prohibition adopting the Secretary of State's Findings of Fact was entered on February 18, 1997.

On February 3, 1999, the Defendant filed a petition pursuant to Chapter 7 of the Bankruptcy Code. On March 9, 1999, the Plaintiffs filed a Complaint to Determine the Dischargeability of Debt pursuant to 11 U.S.C. § 523(a)(2)(A). Much of the Complaint quotes verbatim from the Stipulation and Order entered by the Secretary of State, including the above-referenced failures to disclose.

11 U.S.C. § 523(a)(2)(A) excepts from discharge those debts which have been obtained by "false pretenses, a false representation, or actual fraud". In order for a debt to be found nondischargeable under § 523(a)(2)(A), the plaintiff must prove by a preponderance of the evidence that the defendant knowingly made

a false representation with the intention and purpose of deceiving the creditor, that the creditor relied on the representation, and that the creditor sustained damages as a proximate result of the representation having been made. Field v. Mans, 116 S.Ct. 437, 446 (1995); Grogan v. Garner, 111 S.Ct. 654, 661 (1991); In re Mayer, 51 F.3d 670, 673 (7th Cir. 1995), *cert. denied* 116 S.Ct. 563 (1995); In re Sheridan, 57 F.3d 627, 635 (7th Cir. 1995); In re Scarlata, 979 F.2d 521, 525 (7th Cir. 1992); In re Kimzey, 761 F.2d 421, 423-24 (7th Cir. 1985).

The doctrine of collateral estoppel (issue preclusion) applies to adversary proceedings brought pursuant to 11 U.S.C. § 523(a). Grogan v. Garner, *supra*, 111 S.Ct. *at* 658, n. 11. Under this doctrine, issues determined in a prior state court proceeding may not be re-litigated in the bankruptcy court. Stephan v. Rocky Mountain Chocolate Factory, 136 F.3d 1134, 1136 (7th Cir. 1998); Meyer v. Rigdon, 36 F.3d 1375, 1378 (7th Cir. 1994). However, the bankruptcy court has exclusive jurisdiction to determine the dischargeability of the debts. *See* 11 U.S.C. § 523(c)(1).

In the Seventh Circuit, four requirements must be met in order for collateral estoppel to apply:

1. the issue sought to be precluded must be the same as that involved in the prior litigation;

2. the issue must have been actually litigated;

3. the determination of the issue must have been essential to the final judgment; and

4. the party against whom estoppel is invoked must be fully represented in the prior action.

Meyer v. Rigdon, *supra*, 36 F.3d *at* 1379; Klingman v. Levinson, 831 F.2d 1292, 1295 (7th Cir. 1987).

The Bankruptcy Court is required to give an Illinois state court judgment the same full faith and credit as they have by law or usage in the Illinois courts. 28 U.S.C. § 1738. Accordingly, this Court is required to give preclusive effect to Illinois state court judgments whenever the Illinois courts would do so. In re Winston, 114 B.R. 566, 571 (Bankr. N.D. Ill. 1990). The issue here is whether Illinois would give the Secretary of State's Consent Order of Prohibition preclusive effect against claims asserted in the bankruptcy.

The Defendant argues that the "actually litigated" requirement of collateral estoppel has not been met in this case. The Defendant correctly notes that consent judgments are generally not given preclusive effect in subsequent court proceedings. As the Seventh Circuit noted in La Preferida v. Cerveceria Modelo, S.A. de S.V., 914 F.2d 900, 906 (7th Cir. 1990):

> [C]onsent judgments, while settling the issue definitively between the parties, normally do not support an invocation of collateral estoppel (citations omitted). The rationale behind this general rule is that issues underlying a consent judgment generally are neither actually litigated nor essential to the judgment.

See Meyer v. Rigdon, *supra*, 36 F.3d *at* 1379.

There is an exception to the general rule that consent judgments are not given preclusive effect in subsequent proceedings. Where "the parties could reasonably have foreseen the conclusive effect of their actions", collateral estoppel may be

applied to consent decrees. Klingman v. Levinson, *supra*, 831 F.2d *at* 1296, *quoting* 1B J. Moore, J. Lucas & T. Currier, *Moore's Federal Practice* ¶ 0.444[1] *at* 794 (2d ed. 1984). The facts in this case do not warrant a departure from the general rule forbidding the application of collateral estoppel to consent judgments. The only relief sought in the prior administrative proceeding was an order prohibiting the Defendant from offering or selling securities in the State of Illinois. There is no evidence that the Defendant planned on selling securities in the future, and thus he may have had little or no incentive to defend himself in the administrative proceeding. No money judgment was sought or awarded in the administrative proceeding. Under these circumstances, the record does not clearly establish that the parties intended the fraud issues to be foreclosed in future litigation.

For the foregoing reasons, the Plaintiffs' Motion for Collateral Estoppel is denied.

This Opinion is to serve as Findings of Fact and Conclusions of Law pursuant to Rule 7052 of the Rules of Bankruptcy Procedure.

See written Order.

ENTERED: August 1, 2000

_____
LARRY LESSEN
UNITED STATES BANKRUPTCY JUDGE

c: Michael J. Logan
837 S. 4th St.
Springfield, IL 62703

William E. Jarvis
108 S. 5th St.
Auburn, IL 62615

U.S. Trustee
401 Main St. #1100
Peoria, IL 61602

CERTIFICATION OF MAILING

The undersigned, deputy clerk of the United States Bankruptcy Court, hereby certifies that a copy of this Opinion was mailed this date to the parties listed herein.

Dated: August 1, 2000 _____

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	)	
THOMAS L. FOLDER,	)	
	)	
Defendant.	)	

O R D E R

For the reasons set forth in an Opinion entered this day,

IT IS HEREBY ORDERED that the Plaintiffs' Motion for Collateral Estoppel filed April 24, 2000, be and is hereby denied.

ENTERED: August 1, 2000

_____
LARRY LESSEN
UNITED STATES BANKRUPTCY JUDGE

c: Michael J. Logan
837 S. 4th St.
Springfield, IL 62703

William E. Jarvis
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